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Research Update: Exelon Corp. And Units Corporate Credit Ratings Cut To 'BBB+', Still On Watch Neg

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 Primary Credit Analyst: John Kennedy, New York (1) 212-438-7670;
 john_kennedy@standardandpoors.com

Credit Rating: BBB+/Watch Neg/A-2

Rationale

On Oct. 3, 2005, Standard & Poor's Ratings Services lowered its corporate credit rating on diversified energy company Exelon Corp. and its subsidiaries to 'BBB+' from 'A-'. The 'A-2' short-term corporate credit ratings remain unchanged.

The ratings on all Exelon affiliates remain on CreditWatch with negative implications pending the completion of the merger with Public Service Enterprise Group Inc. (BBB/Watch Dev/A-3).

As of June 30, 2005, the Chicago, Ill.-based company had \$10 billion of debt outstanding.

The rating action for Exelon and its affiliates recognizes the heightened adversarial regulatory environment in Illinois, the potential impact of cash flow degradation at Commonwealth Edison Co. on the consolidated entity, and Standard & Poor's view that final regulatory resolution of this dispute will weaken credit protection measures to a level more appropriate with the lower rating. Prior to the merger announcement in December 2004, the ratings on the Exelon companies had borne negative outlooks precisely for the regulatory uncertainties facing Commonwealth Edison in 2007, when the rate freeze expires and rules for the new rate structure and power procurement process are needed.

The regulatory climate in Illinois has suddenly become exceptionally politicized and uncertain and may lead to debilitating rate decisions should a constructive settlement that allows for the timely recovery of all costs of providing service not be achieved before the rate freeze expires in 2007. The actions of Illinois' governor, first publicly denouncing the staff recommendation for a rate increase at Commonwealth Edison to recover costs and, second, replacing the chairman of the Illinois Commerce Commission with the public advocate who also played an advocacy and participatory role in the post-2006 procurement proceedings reveal a position that is unsupportive of Exelon's credit quality. In addition, Exelon's escalation of the hostilities by threatening a future bankruptcy at Commonwealth Edison has heightened credit concern.

At present, the Illinois governor's position is to prevent Commonwealth Edison from raising electric rates in 2007. Moreover, strident opposition to rate increases throughout the legislative process portends difficulties Commonwealth Edison may encounter in future regulatory proceedings. Given the large amount of capital expenditures incurred by Commonwealth Edison for infrastructure improvements and because the company's base rate freeze precludes recovery of these expenditures until at least 2007, a regulatory solution is needed that addresses recovery in a manner that does not further impair credit quality.

The ratings on Exelon reflect its relationship with its primary subsidiaries, including its regulated utilities, Commonwealth Edison and PECO Energy Co., and nonregulated Exelon Generation Co. LLC, as well as its other nonregulated diversified businesses. Exelon's satisfactory

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business profile is supported by the utilities' low-risk electric and gas transmission and distribution operations, the low production costs of the company's nuclear-fired assets, strong transmission links to the Mid-American Interconnected Network and Mid-Atlantic Area Council regions. Historically, restructuring rulings for Commonwealth Edison and PECO Energy in their respective states have minimized the financial risks related to their old nuclear assets by providing an accelerated recovery of the related capital invested in these facilities.

The senior secured ratings at subsidiaries Commonwealth Edison and PECO Energy were unchanged at 'A-' reflecting Standard & Poor's assessment of the security package, which determined there is sufficient collateral to support the current rating level.

Short-term credit factors

The short-term rating on Exelon is 'A-2'. During the short term, Standard & Poor's expects cash flow from operations to fully fund maintenance capital expenditures and dividends, despite the potential for material discretionary pension contributions due to the company's underfunded postretirement obligations. The company's cost-reduction program should meaningfully contribute to cash flow, and the its business profile will marginally strengthen as Exelon continues its efforts to sell many of its remaining nonregulated, diversified businesses. However, the expiration of Commonwealth Edison's full-requirements contract in 2006 creates tremendous uncertainty for the consolidated entity. Thus, developments along the regulatory front will be a key credit driver during the short term.

Exelon's liquidity should adequately support working capital needs throughout the year, assuming the company continues to prudently manage risk, particularly at Exelon Generation. Exelon has access to a \$500 million revolving credit facility that matures in October 2006, a \$1 billion facility that matures in July 2009, and about \$545 million of cash and cash equivalents as of June 30, 2005. The company and its subsidiaries meet their short-term liquidity needs with commercial paper, which the credit facilities back up. As of June 30, 2005, there was \$329 million of commercial paper outstanding.

Other points of note regarding the company's liquidity include:

- None of Exelon's or its subsidiaries' borrowings are subject to default or prepayment due to a rating downgrade of its securities.
- Aside from securitized debt--the interest and principal payments of which are recovered through rates--the company maintains a reasonable debt maturity profile.
- Failure to maintain an investment-grade rating would allow some of Exelon Generation's counterparties to terminate derivatives and settle transactions on a net present value basis.

Ratings List

Ratings Lowered, Still On Watch Neg

	To	From
Exelon Corp.		
Long-term corp credit rtg	BBB+/Watch Neg	A-/Watch Neg
Sr unsec'd debt	BBB/Watch Neg	BBB+/Watch Neg
Commonwealth Edison Co.		
Long-term corp credit rtg	BBB+/Watch Neg	A-/Watch Neg
Sr unsec'd debt	BBB/Watch Neg	BBB+/Watch Neg

Exelon Generation Co. LLC

Long-term corp credit rtg	BBB+/Watch Neg	A-/Watch Neg
Sr unsecd debt	BBB+/Watch Neg	A-/Watch Neg

Peco Energy Co.

Long-term corp credit rtg	BBB+/Watch Neg	A-/Watch Neg
Sr unsecd debt	BBB/Watch Neg	BBB+/Watch Neg
Preferred stock	BBB-/Watch Neg	BBB/Watch Neg

Ratings Still On Watch Neg

Exelon Corp.

Short-term corp credit rtg	A-2/Watch Neg
Commercial paper	A-2/Watch Neg

Commonwealth Edison Co.

Short-term corp credit rtg	A-2/Watch Neg
Commercial paper	A-2/Watch Neg
Senior secured debt	A-/Watch Neg

Exelon Generation Co. LLC

Short-term corp credit rtg	A-2/Watch Neg
Commercial paper	A-2/Watch Neg

Peco Energy Co.

Short-term corp credit rtg	A-2/Watch Neg
Commercial paper	A-2/Watch Neg
Senior secured debt	A-/Watch Neg

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